United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLANT

Signed

76-6153

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

B
P/S

FRANK A. DELORENZO,

Plaintiff-Appellee

v.

UNITED STATES OF AMERICA,

Defendant-Appellant

ON APPEAL FROM THE JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF NEW YORK

BRIEF FOR THE APPELLANT

SCOTT P. CRAMPTON,
Assistant Attorney General,

GILBERT E. ANDREWS,
RICHARD W. PERKINS,
JOHN G. MANNING,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

Of Counsel:

JAMES M. SULLIVAN, JR.,
United States Attorney.

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STATEMENT OF THE ISSUE PRESENTED

Whether the District Court erred in determining that the taxpayer, a bookmaker, was liable for wagering excise taxes for only 20 days of the 56-day period for which those wagering taxes were assessed.

STATEMENT OF THE CASE

This is an appeal by the United States of America from a judgment of the United States District Court for the Northern District of New York, dismissing a complaint in a civil action brought by Frank A. DeLorenzo (taxpayer) against the United States for a refund of $599.01 paid by taxpayer in partial satisfaction of assessments of federal wagering excise taxes, penalties and interest in the aggregate amount of $14,734.92 (R. 77, 81; Compl. par. 11.)[1/] The judgment also ordered that the Government was entitled to recover $2,801.44 from taxpayer on a counterclaim for $10,956.50, representing the unpaid balance of the assessments. (R. 81; Ans. and Counterclaim, p. 3.)[2/] The judgment was entered on July 9, 1976, pursuant to a memorandum-decision and order (R. 75-81) of the same date reported at 76-2 U.S.T.C., par. 16,230 (R. 2). The Government filed a timely notice of appeal on September 2, 1976. (R. 2.) The material facts, as found by the District Court and as otherwise reflected on the record, may be summarized as follows:

1/ "R." references are to the separately bound record appendix.

2/ In its counterclaim, the Government asserted that taxpayer had made payments aggregating $983.05 in satisfaction of the assessments and that the assessment of $2,795.37 in penalties had been abated, thus reducing the unpaid balance of the outstanding assessments to $10,956.50. In its post-trial brief the Government acknowledged that further payments by taxpayer had increased the total collected by the Government on the assessments to $1,192.66, thereby decreasing the unpaid balance of the assessments to $10,746.89. (R. 77.)

On August 1, 1967, taxpayer was placed under surveillance by the New York State Police on suspicion of being involved in illegal gambling activities. During the ensuing two months an undercover investigator for the State Police observed taxpayer about two out of every three days. On September 26, 1967, the surveillance was terminated, and on October 4 taxpayer was arrested on criminal gambling charges. (R. 10-11, 16-19, 76.)

At the time of his arrest, the policy found an envelope on taxpayer's person containing $284 in cash and betting slips on which $434.75 of wagers were recorded. On the same day as he was arrested, the police also raided a clothing store owned by the taxpayer. There they arrested an employee of the store on criminal gambling charges and seized from a desk drawer on the premises a quantity of betting slips on which $1,563.47 of wagers were recorded. (R. 46, 56, 61, 76; Tr. 13-14, 68-69, 73-77, 90-92; Ex. D.)

Upon learning of the raid through a local newspaper, Peter Letko, a revenue agent with the Internal Revenue Service, commenced an investigation of taxpayer's liability for the federal excise tax on wagers. The revenue agent determined that $1,996.72 of the wagers recorded on the betting slips found on his person and in the desk drawer at his clothing store were placed with taxpayer on the day of his arrest.[3/] Using this

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3/ The wagers recorded on the betting slips totaled $1,998.22 or only $1.50 more than the $1,996.72 in bets determined by the revenue agent to have been placed with taxpayer on the day of his arrest. (Ex. D.) The reason for the difference in amounts is not explained by the record.

figure as a representative day's wagers placed with taxpayer, the revenue agent further determined that the total amount of taxable wagers placed with taxpayer during the months of August through October, 1967, equalled $111,815.26 or approximately $1,996.72 multiplied by 56, the number of days, except for Sundays, in the period between taxpayer's arrest and the first day he was placed under surveillance. (R. 40-43, 46, 48, 56-58, 61, 76; Ex. D.)

After assessments were made pursuant to these determinations, taxpayer paid a portion of the taxes assessed and filed a claim for refund of the portion paid and for abatement of the outstanding balance. (Compl. pars. 5-7; Ans. pars. 5-6; Compl. Ex. A.) Following the denial of the claim by the Internal Revenue Service, taxpayer commenced the instant action. (R. 2; Compl. par. 9.)[4/]

In its memorandum decision and order the District Court sustained the revenue agent's determination that the wagers accepted by taxpayer on the day of his arrest consisted of the wagers recorded on the betting slips seized from the desk drawer

4/ Although taxpayer's claim for refund and abatement and his action in the District Court for a refund were based on the premise that he had not accepted any wagers during the months in question, he admitted at trial that he had taken $10,000 in bets during that period. (R. 6.) In his post-trial brief (p. 10), taxpayer further conceded that he had accepted a total of $12,042.50 in wagers during the same period and that the resulting 10 percent tax ($1,204.25) exceeded the $1,192.66 paid by him by $11.59.

at his clothing store, as well as those recorded on the betting slips found on his person. (R. 78.) Notwithstanding taxpayer's testimony at trial (R. 7-8) that he had taken bets every working day between the date of his arrest and the first day he was placed under surveillance, the District Court also determined, however, that the revenue agent's computation of the number of days that taxpayer had accepted wagers was erroneous (R. 78-80). It found that the revenue agent held intended to base his computation not on the number of working days in the period prior to his arrest that taxpayer was generally under surveillance, but on the number of days in that period that taxpayer was actually seen by state law enforcement personnel. (R. 78-79, 80.) It further found that taxpayer was observed on only twenty occasions, once on the day of his arrest, and nineteen times (or one out of every three days) during the time (August 1 to September 26) the undercover investigator had him under surveillance. (R. 79, 80.) In accordance with these findings, the District Court concluded that the revenue agent should have computed taxpayer's excise tax liability on the basis of 20 days' bookmaking and that the revenue agent's determination that taxpayer took bets on each of 56 days reflected his mistaken belief as to the number of days that taxpayer was actually seen by state law enforcement personnel. (R. 77-78, 80.) Following the entry of judgment in conformity with this conclusion, the Government took this appeal.

ARGUMENT

THE DISTRICT COURT ERRED IN DETERMINING THAT THE NUMBER OF DAYS TAXPAYER WAS ENGAGED IN ACCEPTING TAXABLE WAGERS SHOULD HAVE BEEN COMPUTED ON THE BASIS OF THE NUMBER OF DAYS THAT TAXPAYER WAS ACTUALLY OBSERVED BY STATE LAW ENFORCEMENT PERSONNEL RATHER THAN ON THE BASIS OF THE NUMBER OF DAYS THAT TAXPAYER ADMITTED HE WAS TAKING BETS

As it existed in 1967, Section 4401(a) of the Internal Revenue Code of 1954, Appendix, infra, imposed a 10 percent (now 2 percent)[5/] excise tax on wagers. Under Sections 4401(c) and 4403 of the Code, Appendix, infra, every person engaged in the business of accepting wagers is liable for the tax on all wagers placed with him and is required to keep a daily record showing the gross amount of such wagers. If, as in the instant case, a person fails to keep a daily record of all wagers placed with him, as required by statute, the Commissioner of Internal Revenue is authorized to estimate the amount of wagers placed with such person by any reasonable method in order to compute his tax liability. See Hamilton v. United States, 309 F. Supp. 468, 473 (S.D. N.Y., 1969), aff'd per curiam, 429 F. 2d 427 (C.A. 2, 1970); United States v. Firtel, 446 F. 2d 1005, 1006-1007 (C.A. 5, 1971). Cf. United States v. Lowder, 492 F. 2d 953, 956 (C.A. 4, 1974), cert. denied, 419 U.S. 1092 (1974); Foster v. Commissioner, 487 F. 2d 902, 903 (C.A. 6, 1973); Mendelson v. Commissioner, 305 F. 2d 519, 523 (C.A. 7, 1962), cert. denied, 371 U.S. 887 (1962). Furthermore, where a taxpayer contests the

5/ See Internal Revenue Code of 1954, Sec. 4401(a), as amended by Sec. 3(a), Act of October 29, 1974, P.L. 93-499, 88 Stat. 1549.

Commissioner's reconstruction of wagers in a suit for refund of any portion of the resulting tax paid, the taxpayer's burden of proof, as the District Court here recognized (R. 77), is not merely to show that the Commissioner's assessment of taxes pursuant to his reconstruction is in error, but is to show the correct amount of tax owed. See United States v. Janis, 44 U.S. Law Week 5303, 5305-5306 (Sup. Ct., July 6, 1976); Helvering v. Taylor, 293 U.S. 507, 514 (1935); Psaty v. United States, 442 F. 2d 1154, 1158-1159 (C.A. 3, 1971); Mersel v. United States, 420 F. 2d 517, 518 (C.A. 5, 1969); Compton v. United States, 334 F. 2d 212, 216 (C.A. 4, 1964). Moreover, the taxpayer has the same burden of proof with respect to the Government's counterclaim for any unpaid portion of the taxes assessed. See Lesser v. United States, 368 F. 2d 306, 310 (C.A. 2, 1966) (en banc); Psaty v. United States, supra, pp. 1158-1161; United States v. Rexach, 482 F. 2d 10, 15-18 (C.A. 1, 1973), cert. denied, 414 U.S. 1039 (1973); Liddon v. United States, 448 F. 2d 509, 514 (C.A. 5, 1971), cert. denied, 406 U.S. 918 (1972). Cf. United States v. Janis, supra, pp. 5305-5306.

In the instant case, as indicated above, Revenue Agent Letko reconstructed the amount of taxable wagers placed with taxpayer in the months of August through October, 1967, by first determining the amount of wagers placed with taxpayer on the day of his arrest. Using this figure as a representative day's wagers, the revenue agent then determined the total amount of taxable wagers by multiplying this figure by 56, or the number of days,

except for Sundays, between taxpayer's arrest and the first day he was placed under surveillance. (R. 41-43, 48, 56-58, 61, 76; Ex. D.)

The District Court, however, found that the revenue agent had intended to base his computation of taxpayer's taxable wagers on the number of days that taxpayer was actually observed by state law enforcement personel and had mistakenly believed that taxpayer was under surveillance on 56 separate occasions. (R. 77-80.) Accordingly, the District Court concluded that the revenue agent erroneously determined the number of days that taxpayer had accepted wagers. (R. 78-80.) It is this conclusion of the District Court that is plainly in error and that forms the basis of the Government's appeal.

First of all, although the revenue agent testified (R. 42-43, 50-51) that he based his calculation of the number of days that wagers were placed with taxpayer on the time that taxpayer was under surveillance, the surveillance time referred to did not mean the actual number of days on which taxpayer was seen by state law enforcement personnel, but the period of time between his arrest and the first day he was placed under surveillance. This is made clear by the fact that the revenue agent also testified (R. 51-52) that he would not have altered his determination of the number of days that taxpayer had taken bets if he had known that the undercover investigator observed taxpayer

only about two out of every three days in the period taxpayer was under surveillance.[6/]

In any event, the revenue agent's determination that taxpayer had accepted wagers on 56 days, or on each day except Sunday in the period between the day of his arrest and the first day he was placed under surveillance was corroborated by the testimony at trial of the taxpayer himself (R. 7-8) that he took bets on every working day, i.e., on five or six days out of every week, in the same period. Accordingly, on the basis of the taxpayer's own testimony, the District Court clearly erred in finding (R. 79) that the 56 days calculated by the revenue agent "was not shown to be rationally based on any fact recited during * * * [the] hearing." Therefore, the amount of wagers found by the District Court to have been placed with taxpayer on the day of his arrest was properly projected over the 56 days the taxpayer admitted to having been engaged in book-

6/ In addition to misinterpreting the revenue agent's testimony that his calculation of the number of days that taxpayer had accepted wagers was based on the time that taxpayer was under surveillance, the District Court apparently made an inadvertent error in finding that the undercover investigator observed taxpayer only 19 times, or one out of every three days during the surveillance period. According to that undercover investigator's testimony (R. 18-19), one out of every three days was the frequency during the surveillance period that he failed to observe the taxpayer. Thus, taxpayer was actually seen by him about two out of every three days during the surveillance period.

making, rather than the 20 days[7] the District Court found taxpayer was observed by state law enforcement personnel. See Heyman v. United States, 497 F. 2d 121, 122-123 (C.A. 5, 1974); United States v. Washington, 251 F. Supp. 359 (E. D. Va., 1966), aff'd, 402 F. 2d 3 (C.A. 4, 1968), cert. denied, 402 U.S. 978 (1971); O'Neill v. United States, 198 F. Supp. 367, 370-371 (E.D. N.Y., 1961). Cf. Hamilton v. United States, supra, pp. 472-473.

7/ As indicated in footnote 6, p. 9, supra, this finding reflects the mistaken belief of the district judge that the undercover investigator observed taxpayer only 19 times, or one out of every three days during the surveillance period. As the investigator actually saw taxpayer about 38 times, or two out of every three dyas during the surveillance period (see R. 18-19), according to the District Court's own analysis of the case, it should have found that, including the day of his arrest, taxpayer was seen by state law enforcement personnel on a total of 39 days.

CONCLUSION

For the foregoing reasons, the judgment of the District Court should be reversed and the cause remanded with instructions to enter judgment for the United States on its counterclaim to the extent the amount sought therein has not been paid.

Respectfully submitted,

SCOTT P. CRAMPTON,
Assistant Attorney General,

GILBERT E. ANDREWS,
RICHARD W. PERKINS,
JOHN G. MANNING,
Attorneys,
Tax Division,
Department of Justice,
Washington, D.C. 20530.

Of Counsel:

JAMES M. SULLIVAN, JR.,
United States Attorney.

NOVEMBER, 1976.

CERTIFICATE OF SERVICE

It is hereby certified that service of this brief has been made on opposing counsel by mailing four copies thereof on this 17th day of November, 1976, in an envelope, with postage prepaid, properly addressed to him as follows:

Davis M. Etkin, Esquire
Etkin and Stark
833 Union Street
Schenectady, New York 12308

Gilbert E. Andrews/cas
GILBERT E. ANDREWS
Attorney.

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 4401. IMPOSITION OF TAX.

(a) Wagers.--There shall be imposed on wagers, as defined in section 4421, an excise tax equal to 10 percent of the amount thereof.

* * *

(c) [as amended by Sec. 151(a), Excise Tax Technical Changes Act of 1958, P.L. 85-859, 72 Stat. 1275] Persons Liable for Tax.--Each person who is engaged in the business of accepting wagers shall be liable for and shall pay the tax under this subchapter on all wagers placed with him. Each person who conducts any wagering pool or lottery shall be liable for and shall pay the tax under this subchapter on all wagers placed in such pool or lottery. Any person required to register under section 4412 who receives wagers for or on behalf of another person without having registered under section 4412 the name and place of residence of such other person shall be liable for and shall pay the tax under this subchapter on all such wagers received by him.

SEC. 4403. RECORD REQUIREMENTS.

Each person liable for tax under this subchapter shall keep a daily record showing the gross amount of all wagers on which he is so liable, in addition to all other records required pursuant to section 6001(a).